

## Message Text

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ACTION ARA-14

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FM AMEMBASSY PANAMA

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EO 11652: N/A

TAGS: ECON, XM

SUBJECT: ECONOMIC ALERT REPORT

REF: (A) STATE 180067; (B) PANAMA A-103

1. SUMMARY: THIS MESSAGE CONTAINS INFORMATION REQUESTED IN REFTEL (A). THE PANAMANIAN ECONOMY CONTINUES STAGNANT WITH LITTLE LIKELIHOOD OF SIGNIFICANT RECOVERY IN THE NEAR FUTURE IN THE ABSENCE OF A NEW TREATY CONTAINING A GENEROUS ECONOMIC PROVISION AND WITHOUT SIGNIFICANT IMPROVEMENT IN SUGAR PRICES ENABLING PANAMA TO EXPORT AT A PROFIT. END SUMMARY.

2. REQUESTED INFORMATION FOLLOWS:

A. MAJOR ECONOMIC PROBLEMS: CONTINUING ECONOMIC PROBLEMS HAVE KEPT PANAMA FROM RECOVERING FROM THE 1974 RECESSION. THESE PROBLEMS INCLUDE HIGH UNEMPLOYMENT, PARTICULARLY IN THE COLON AREA, DEFICIT OPERATION OF THE LARGE NEW GOVERNMENT-OWNED SUGAR MILLS, SLUGGISH ACTIVITY IN CONSTRUCTION AND OTHER BASIC INDUSTRIES, CONTINUED HIGH COST OF PETROLEUM IMPORTS, UNCERTAINTIES OVER THE ECONOMIC PROVISIONS AND THE LIKELY EFFECT OF A POSSIBLE NEW TREATY, AND, PARTICULARLY, PANAMA'S GROWING INTERNATIONAL DEBT AND DEBT-SERVICING REQUIREMENTS. THE GOP HAS BEEN

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UNABLE TO AFFORD TO KEEP PUTTING ENOUGH MONEY INTO PUBLIC WORKS PROJECTS FAST ENOUGH TO TAKE UP THE SLACK CAUSED BY INVESTOR RELUCTANCE IN THE PRIVATE SECTOR. FURTHERMORE, LABOR COSTS WHICH GENERALLY ARE HIGHER THAN IN NEIGHBORING COUNTRIES MAKE EXPORT COMPETITION DIFFICULT. SINCE THE RISE TO POWER OF THE PRESENT REGIME, THE GOP HAS COMMITTED ITSELF TO A POPULAR POLICY OF IMPROVING THE LOT

OF THE POOR, THE WORKERS, AND THE PEASANT FARMERS, THROUGH RURAL AND URBAN DEVELOPMENT PROGRAMS, IMPROVED EDUCATION AND HEALTH FACILITIES, ROADS, LOW-COST HOUSING, ETC.--ALL POPULAR PROJECTS BUT WHICH, OF COURSE, HAVE NOT GENERATED MUCH INCOME TO HELP AMORTIZE COSTS. TWO LARGE AND COSTLY GOVERNMENT-OWNED SUGAR MILLS WHICH WERE DESIGNED TO HELP RELIEVE PANAMA'S FOREIGN TRADE IMBALANCE HAVE NOW BEEN COMPLETED AND COME INTO PRODUCTION AT A TIME WHEN INTERNATIONAL SUGAR PRICES HAVE DROPPED TO 7 1/2 CENTS A POUND, BARELY HALF THE BREAK-EVEN PRICE. BECAUSE DOMESTIC CONSUMPTION AND CAPITAL INVESTMENT HAVE CONSIDERABLY EXCEEDED PRODUCTION IN RECENT YEARS, PANAMA'S NATIONAL DEBT, PARTICULARLY FOREIGN DEBT, HAS GREATLY INCREASED, WITH DEBT-SERVICING REQUIREMENTS ABSORBING AN EVER-INCREASING PORTION OF GOVERNMENT REVENUES. DEBT SERVICE REQUIREMENTS FOR 1977 ARE ESTIMATED AT \$110 MILLION, OR ABOUT 33 PERCENT OF CENTRAL GOVERNMENT REVENUES. IN ADDITION, DEBT SERVICE OF SEMI-AUTONOMOUS AGENCIES WILL BE ABOUT \$55 MILLION, A PORTION OF WHICH THE CENTRAL GOVERNMENT WILL PROBABLY HAVE TO PICK UP.

B. TWELVE-MONTH OUTLOOK. THERE ARE FEW INDICATIONS SUGGESTING ANY QUICKENING OF THE ECONOMY IN THE NEXT TWELVE MONTHS, BARRING THE PSYCHOLOGICAL EFFECT THAT THE POSSIBLE SIGNING A A TREATY WOULD HAVE. STATISTICS INDICATE A SLIGHT (TWO PERCENT) INCREASE IN INDUSTRIAL EMPLOYMENT IN THE FIRST QUARTER OF 1977 OVER THE FIRST QUARTER OF 1976; LIMITED OFFICIAL USE

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THIS INCREASE MAY SIGNAL A REVERSE IN THE STEADILY DOWNWARD TREND IN EMPLOYMENT OBSERVED SINCE 1974, ALTHOUGH IT IS STILL LESS THAN THE GROWTH OF THE POPULATION AS A WHOLE. RETAIL SALES REPORTED FIRST QUARTER INCREASES OF MORE THAN TEN PERCENT ABOVE THE CORRESPONDING PERIOD OF 1976, ALTHOUGH IT IS GENERALLY AGREED THAT THIS IS NOT EVIDENCE OF A NEW TREND BUT RATHER THE EFFECT OF ELEVENTH-HOUR PURCHASING TO BEAT THE MARCH 1 EFFECTIVE DATE OF THE NEW VALUE-ADDED TAX (ITBM). AGRICULTURAL PRODUCTION MAY SHOW SOME IMPROVEMENT OVER 1976, ALTHOUGH THE MAY RAINS WERE AGAIN SLOW IN ARRIVING THIS YEAR. MOST GRIM IS THE OUTLOOK FOR FOREIGN DEBT IN 1978, WHEN DEBT-SERVICING REQUIREMENTS FOR ALREADY-EXISTING COMMITMENTS WILL REACH ABOUT \$200 MILLION. PANAMA'S MAIN HOPE FOR RELIEF, BEYOND THE EFFECT OF SIGNING A FAVORABLE TREATY, LIES IN THE POSSIBILITY OF A SIGNIFICANT RISE IN INTERNATIONAL SUGAR PRICES, AN UNLIKELY EVENT IN THE ABSENCE OF A MEANINGFUL SUGAR AGREEMENT. THE SIGNING OF A NEW CANAL TREATY MAY PROVIDE A PSYCHOLOGICAL BOOST, BUT ANY PERSISTENT UNFAVORABLE NOISES FROM WASHINGTON ON RATIFICATION PROSPECTS COULD DISSIPATE IT.

C. CRITICAL POINTS. THERE ARE THREE CRITICAL POINTS WHICH COULD AFFECT THE FINANCIAL CONDITION OF THE GOP AND HENCE THE ECONOMY OF THE COUNTRY. THESE ARE A NEW TREATY, DEBT RESCHEDULING, AND EXPORT SALES OF SUGAR. PANAMA, LIKE MANY OTHER LDC'S, IS PROBABLY NEAR THE LIMIT OF ITS BORROWING ABILITY AND MAY FIND DIFFICULTY IN OBTAINING CONTINUED FINANCING THROUGH THE IFI'S AS WELL AS THE COMMERCIAL BANKS IF ITS LARGE ADVERSE TRADE BALANCE PERSISTS. CRITICAL POINTS WHERE US POLICY MAY BE EFFECTIVE ARE (1) THE SIGNING--AND SUBSEQUENT RATIFICATION--OF A TREATY WHICH CONTAINS A SUFFICIENTLY GENEROUS ECONOMIC PROVISION TO EASE PANAMA'S DEBT-SERVICING LOAD AND INCREASE ITS CREDITWORTHINESS IN THE EYES OF THE BIG LENDERS, (2) ASSISTANCE THROUGH ENCOURAGING PRIVATE U.S. BANKS TO RELIMITED OFFICIAL USE

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SCHEDULE PANAMANIAN DEBT REPAYMENTS, AND (3) AN INTERNATIONAL, OR BILATERAL, SUGAR AGREEMENT WHICH WILL ENABLE PANAMA TO EXPORT SUBSTANTIAL QUANTITIES OF SUGAR AT A REASONABLE PROFIT.

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